

Master Document – Audit Planning

Activity Code 17600	Financial Capability, Modified Financial Condition Risk Assessment
Version 1.3, dated April 2003	
B-1	Planning Considerations
Purpose and Scope	
The objective is to perform a modified risk assessment as addressed in CAM 14-303 and 304. A modified risk assessment consist of the calculation and analysis of the trend of the contractor's key financial ratios shown in CAM 14-304 and an analysis of any significant events of which the auditors become aware that would impact the contractor's financial status.	
References	
1. DFARS 232.072, "Financial Responsibility of Contractors"	
2. SAS 59, "The Entity's Ability to Continue as a Going Concern"	
3. CAM 14-304, in CAM Chapter 14 "Financial Condition Risk Assessment Procedures"	

B-1	Preliminary Steps
Version 1.3, dated April 2003	
	WP Reference
1. Check the permanent files for prior financial capability audits or risk assessments. Evaluate the audit opinion or memorandums for record to determine if financial distress exists. If the prior audit report had an unfavorable or adverse opinion, a modified risk assessment cannot be performed. If the prior year audit opinion is acceptable or a detailed risk assessment disclosed no significant indicators, then the modified risk assessment should be performed. Note: In accordance with CAM 14-303, a modified risk assessment can be performed only two years in a row. The third year, a detailed risk assessment should be performed.	
2. Conduct an entrance conference with the contractor in accordance with CAM 4-302.	
3. Obtain a copy of the contractor's last fiscal year end financial data and the quarterly interim data (if more than one quarter has passed). Ask	

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<p>the contractor if there are any significant events that have occurred (sale of a division, loss of a contract, large layoff, new contract, buying larger plant, etc.). Since this is a modified risk assessment, a detailed risk assessment/audit or modified risk assessment had to have been performed in the previous year so prior year financial data should already be included in a spreadsheet.</p>	
<p>4. Input the last year and interim year-to-date quarterly financial statement data (if more than one quarter has passed) into an Excel workbook. If the Excel workbook is available from the prior assignment, it may be copied into and used in the assignment. An Excel workbook which calculates financial ratios is available on the Eastern Region website. Use of that workbook is not required, but should improve the efficiency and effectiveness of the modified risk assessment.</p>	
<p>5. Calculate the contractor's key financial ratios shown in CAM 14-304. The Excel workbook should calculate the ratios for the working papers. Per CAM 14-304c.(1), a comparison to industry averages does not need to be performed for a modified risk assessment.</p> <p>Once the financial data is input into the workbook and the key financial ratios are calculated, analyze the trends of the ratios for significant unfavorable changes related to financial distress. This may involve an analysis of the trends of the financial statement data that is used to calculate the ratios. Compare the contractor's current financial data to its own historical data, available in prior year financial capability audit files. Current company ratios should not be compared to industry average ratios.</p> <p>Document whether there are any significant unfavorable or adverse trends that would have an impact on the contractor's financial status that require the performance of a detailed financial condition risk assessment.</p>	
<p>6. Analyze any significant events of which the auditor becomes aware that would impact the contractor's financial status (newspaper article, loss of a contract, major layoff, sale of a division, etc.). This may include discussion with the supervisor or auditor that normally works at the contractor location. Look at the audit lead sheet file or ICQ/ICAPS Summary.</p> <p>Document any significant or unfavorable events that may have an impact on the contractor's financial status that require the performance of a detailed financial condition risk assessment.</p>	
<p>7. In planning and performing the modified risk assessment, consider the fraud risk indicators specific to the audit. The principal sources for the applicable fraud risk indicators are:</p> <ul style="list-style-type: none"> • Listing of Fraud Risk Indicators, Financial Capability 	

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<p>Audits (See APPS Other Audit Guidance Folder for FINCAP-Listing of Fraud Indicators.doc)</p> <p>Document in working paper B any identified fraud risk indicators and your response/actions to the identified risks (either individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed. If no risk indicators are identified, document this in working paper B.</p>	
<p>8. If significant unfavorable or adverse trends or events exist, a detailed risk assessment should be performed under the existing assignment number using the APPS 17600 audit program, Financial Capability Audit. Coordinate with your Supervisory Auditor, discussing the results of the modified financial condition risk assessment and the need to perform a detailed financial condition risk assessment.</p>	
<p>9. If no significant unfavorable or adverse trends or events exist summarize the results of the modified risk assessment in a Memorandum for Record.</p>	

C-1	Detailed Steps	
Version 1.3, dated April 2003		WP Reference
<i>Auditor will develop steps.</i>		
1.		
2.		
3.		
4.		

A-1	Concluding Steps	
Version 1.3, dated April 2003		WP Reference
1. Summarize the results of the modified risk assessment in a Memorandum for Record if no significant unfavorable or adverse trends or events exist. Paragraph 1 is exactly the same as the Subject of Modified Risk Assessment on W/P A-1 and Paragraphs 2 and 3 are exactly the same as the Results of Modified Risk Assessment on W/P A. Once these are updated they, may be copied into the draft memorandum. <i>[If results of this limited evaluation indicate that a detailed financial</i>		

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<i>condition risk assessment needs to be performed, close this assignment and begin a new Working Paper Assignment using a different 17600 code for Financial Capability.]</i>	
2. Coordinate results of modified risk assessment with technical specialist and Supervisory Auditor.	
3. Inform the contractor we are closing our evaluation without further audit and report will not be issued	
4. If the modified risk assessment is performed at a corporate office, distribute a copy of the Memorandum for Record to all FAOs in the CAC network. Include a transmittal letter advising that the memorandum contains sensitive information and should not be released outside of DCAA.	
5. Update permanent files.	
6. Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented (e.g., by initials and date on the CD or working paper folder, etc.) and should include:	
a. If the memo has been electronically transmitted to the customer, scan the signed original memo and file in the working paper package.	
b. Ensure an electronic copy of the final draft memo including the supervisory auditor's initials and date, cross-referenced to the working papers, is included in the working paper package. The final draft memo should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It should differ from the final memo only due to minor administrative changes (spelling, format, etc.) made during final processing.	
c. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.	
d. Two complete sets of electronic working papers must be prepared. The "original" set should be stored in the working paper package. The "archive" set is to be stored separately from the working paper package on a single session CD-ROM. If there will be a short-term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.	
e. Verify that electronic files stored on removable media are not corrupted and can be unarchived.	

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f. Securely enclose the “original” set of electronic files in the working paper package.	
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